

POTENTIAL LIABILITIES OF USING INDEPENDENT CONTRACTORS
BY SUE HUANG & JOI SIMPSON
DHR TOTAL COMPENSATION/SYSTEMS TEAM

Due to the budget reductions, the layoff process has started. As a result, some agencies are considering immediately re-hiring laid-off employees from temporary employment services as independent contractors to perform the same or similar work performed as employees. This practice is not permitted under federal and state law and will expose the state to greater potential liability.

Agencies looking to solve their staffing issues with temporary or contingent workers must consider the legal implications of the employer-employee relationship. Relevant factors must be examined to make sure that this type of action does not create potential liability for the state and agencies. Potential liabilities are as follows:

- Under FLSA, penalties for mischaracterization of an independent contractor could include unpaid overtime or minimum wage, liquidated damages, fines, and criminal sanctions. These could triple if the violation is willful and personal liability could be pursued.
- Under the IRS, a percentage of an agency's payroll could be assessed (this fine could triple if the action is done willfully), as well as FICA penalties and potential litigation settlements.

When considering the utilization of contractors, be aware that converting a state employee or a state temporary employee to an employee performing the same function on a personal service contract could violate state law. CRS 24-18-201 prohibits an employee from being retained via a personal services contract within six months of termination. CRS 24-50-507 prohibits employees from accepting any direct or indirect personal benefit from a contracting agency. In other words, an employee cannot obtain a contract with the state to perform work that he or she had a direct interest in, e.g., the job.

If the state hires laid-off employees within six months to continue to perform the same or similar work prior to lay-off, they cannot be considered independent contractors. These individuals will be eligible for benefits, and could have standing to pursue legal action against the state. In addition to agencies being held liable for flagrant violations of federal and state law, individuals who willfully violate the rule in approving such actions could be held personally liable and incur the same fines and penalties.

Current employees are unlikely to qualify as independent contractors. Here are three key determining factors when qualifying an individual as an independent contractor.

1. Behavior control – Does the employer direct or control how the worker performs the task? Generally, someone who is told when, where and how to perform the work, what tools or equipment to use, what workers to hire, where to purchase supplies, and the order in which to do the work, should not be considered an independent contractor.
2. Financial control – What is the worker's investment in the facilities he or she uses, to what extent is the worker making his or her services available to other organizations, how is the worker paid, and can the worker realize profits and losses from the services provided to the state? If one invests in the facilities and tools used, and if one's service is also available to others, this worker may be considered an independent contractor.
3. Nature of the relationship – Is the organization providing benefits to the worker, are taxes being withheld from the worker's pay, are employer's taxes being paid on behalf

of the worker, is the relationship expected to continue indefinitely, and is the service provided by the worker essential to the regular business of the organization? If so, the worker may not be considered an independent contractor.

The following is the common law test most courts continue to apply.

- The greater the skill required to do the job, the more likely the individual is an independent contractor.
- Individual supplies his or her own tools and materials.
- The longer the relationship, the more likely there is an employer-employee relationship.
- The fact that the person who pays for the work has the right to assign additional projects to the worker without additional compensation and without altering the terms of a contract indicates employee status - an independent contractor relationship is generally contractual.
- An employer who determines the work schedule suggests an employment relationship.
- An individual who is paid by the hour or other time period is more likely to be considered an employee.
- Where the employer hires, fires, and pays the individual's assistant (rather than the worker himself or herself), suggests an employee-employer relationship.
- An individual who works in a field that is not the company's ordinary line of business will be more likely be an independent contractor.
- The fact that a worker is in business for him or herself and has all the appropriate licenses suggests independent contractor status.
- The fact that a worker is treated as an employee for tax purposes indicates an employment relationship.
- Where an individual is integrated into the employer's business to a great extent, the individual is more likely to be considered an employee.
- The establishment of a set amount of work hours suggests employee status.
- The fact that an individual works on the employer's premises suggests employee status.
- An individual who works according to a sequence set by the employer will more likely be deemed an employee.
- An individual who is reimbursed for expenses is more likely an employee.
- An individual's work results in the possible realization of a profit or the risk of a loss suggests independent contractor.
- An individual who works for more than one firm at a time is more likely to be an independent contractor.
- The fact that the employer has the right to discharge the individual suggests an employment relationship.

If an agency were to hire a current state employee (permanent or temporary) to perform the same or similar duties, the agency cannot certify that individual as an independent contractor. Although changing current employees to independent contractors may save some costs, this change would be in violation of federal law, state statute and rules, and will put the state at risk for legal action, heavy fines, and IRS penalties.

Finally, here is some reference material on independent contractors. An article published by the International Personnel Management Association (IPMA) in August 2001 (page 19) states, "Laws governing independent contractors, designed to protect workers from being short-changed, have drawn increasing scrutiny and significance with the growth of the contingent workforce in recent years. Under federal and state laws, an independent

contractor must be just that - independent. He or she must provide a product or service without punching a time clock or being told how to do the job. 'Very few people qualify as independent contractors,' says Eugene Hartwig, an attorney with Butzel Long in Detroit and a former chair of American Bar Association's Section of Labor and Employment Law. One of the key determining factors is behavior control. Does the employer have the right to direct or control how the worker performs the task for which he or she was retained? Generally, someone who is told when and where to do the work, what tools or equipment to use, what workers to hire, where to purchase supplies, and the order in which to do the work, should be classified as a regular employee, not as an independent contractor..."

In the class action lawsuit, *Vizcaino v. Microsoft Corporation*, the court found that Microsoft had mischaracterized certain workers as independent contractors. Such workers were originally hired for specific projects and were not eligible for employee benefits; however, some had been kept on, working on successive projects for a number of years. These employees were fully integrated into Microsoft's workforce, worked on site and on work teams along with Microsoft's regular employees, shared the same supervisors, performed identical functions, worked the same core hours as regular employees, and were provided with admittance card keys, office equipment, and supplies.

For more information contact Sue Huang, Compensation Specialist, 303-866-4219 or Sue.Huang@state.co.us, or Joi Simpson, Personal Services Contracts, 303-866-5496 or Joi.Simpson@state.co.us.

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